

[Release No. 34-35149; File No. SR-OCC-94-08]

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving a Proposed Rule Change Relating to Flexibly Structured Index Options Denominated in a Foreign Currency

December 23, 1994.

On August 19, 1994, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR-OCC-94-08) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").¹ Notice of the proposal was published in the **Federal Register** on October 19, 1994.² No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description of the Proposal

On September 23, 1993, the Commission approved a proposed rule change filed by OCC to accommodate the clearance and settlement of flexibly structured index options.³ Flexibly structured index options exhibit virtually the same characteristics as regular index options; therefore, OCC establishes long and short flexibly structured index option positions in clearing member accounts in precisely the same way it currently does for regular index options. OCC incorporates flexibly structured index options in its premium settlement, margin collection, exercise notice, exercise assignment, and exercise/expiration statement processes without significant changes to those processes. Premiums and exercise prices for the flexibly structured index options that currently are being traded are denominated in United States dollars. Parties to a transaction in such an option may customize certain terms of the option including the expiration date, the exercise style, the exercise price, the cap interval in the case of capped-style options, and the method to be used for establishing the current index value for purposes of settling expiration date exercises.

Recently, the Chicago Board Options Exchange ("CBOE") amended its rules regarding flexibly structured index options⁴ in order to allow premiums

and exercise prices of such options to be denominated in foreign currencies rather than in United States dollars.⁵ Accordingly, OCC is amending its By-Laws and Rules in order to clear and settle these options which OCC calls Flexibly Structured Index Options Denominated in a Foreign Currency ("FX Index Options").

To accommodate the clearance and settlement of FX Index Options, Article XXIII is being added to the Article of OCC By-Laws. Because FX Index Options are a type of index option, the OCC By-Laws governing index options, Article XVII, is being incorporated into new Article XXIII and is being made applicable to FX Index Options. In addition, because FX Index Options will settle in a foreign currency, certain of the OCC By-Laws governing Cross-Rate Foreign Currency Options in Article XX also are being incorporated into new Article XXIII where appropriate. For example, those By-Laws governing extraordinary events, adjustments, and the payment of premiums are being incorporated into the new article.

A Chapter XXIV is being added to the OCC Rules to accommodate FX Index Options. FX Index Options will be exercised pursuant to the rules governing existing index options. Accordingly, the rules governing exercise, assignment, allocation, and the exercise settlement date from Chapter XVIII, which pertains to index options, is being incorporated into new Chapter XXIV. In addition, the settlement procedure for FX Index Options will be the same as the procedure for existing index options. Exercised FX Index Options will be settled through the payment of an exercise settlement amount, which is the difference between the aggregate exercise price and the aggregate current index value. Accordingly, the rules governing exercise settlement and the exercise settlement date from Chapter XVIII are being incorporated into new Chapter XXIV. Because FX Index Options will settle in a foreign currency, certain settlement obligations of a party to an FX Index Option contract will be similar to the settlement obligations of a party to a cross-rate foreign currency option contract. Therefore, certain rules

governing settlement obligations from Chapter XXI, which pertains to cross-rate foreign currency options, are being incorporated into new Chapter XXIV. Specifically, these include the obligation to set up bank accounts and the consequence of failing to pay a foreign currency. Finally, FX Index Options will be margined like cross-rate foreign currency options in that the margin requirement will be calculated in the applicable trading currency and then converted to United States dollars. Consequently, the language of Rule 2111 governing margin requirements for cross-rate foreign currency options is being incorporated into new Chapter XXIV.

Two additional changes to the OCC By-Laws and an additional change to OCC's Rules also are being made. Specifically, the term "FX index option clearing member" is being added to the definition of "clearing member" in Article I, Section 1 of the By-Laws. In addition, the reference to the term "FLEX" in the definition of clearing member is being changed to "flexibly structured option" in order to make that term more generic. Finally, OCC Rule 401 is being amended to require that the currency in which the option is denominated, the expiration date of the option contract as opposed to the expiration month, and the cap price, if any, be included in the Report of Matched Trades.

II. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder and particularly with the requirements of Section 17A(b)(3)(F).⁶ Section 17A(b)(3)(F) requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions, and to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which it is responsible. The Commission believes that OCC's proposed rule change meets these requirements by establishing a framework in which existing OCC systems, rules, and procedures are extended to the processing of the FX Index Options. OCC should be able to implement the clearance and settlement of the FX Index Options without much difficulty because FX Index Options are similar to regular index options and cross-rate foreign currency options currently cleared by OCC. The Commission believes that the use of

93-33] (order approving a proposed rule change relating to FLEX options designated in foreign currencies).

⁵ Premium and exercise prices for these non-United States dollars flexibly structured index options may be denominated in any of the foreign currencies currently underlying foreign currency options. Those currencies include: (1) Australian dollars, (2) British pounds, (3) Canadian dollars, (4) European Economic Community currency units, (5) French francs, (6) German Deutsche marks, (7) Japanese yen, and (8) Swiss francs.

⁶ 15 U.S.C. 78q-1(b)(3)(F) (1988).

¹ 15 U.S.C. 78s(b)(1) (1988).

² Securities Exchange Act Release No. 34837 (October 13, 1994), 59 FR 52852.

³ Securities Exchange Act Release No. 31912 (February 23, 1993), 58 FR 11879 [File No. SR-OCC-92-33] (order approving proposed rule change relating to flexibly structured index options).

⁴ Securities Exchange Act Release No. 34203 (June 13, 1994), 59 FR 31658 [File No. SR-CBOE-

OCC's systems for the clearance and settlement of FX Index Options should facilitate promptness and precision.

III. Conclusion

The Commission finds that the proposal is consistent with the requirements of the Act, particularly with Section 17A(b)(3)(F) of the Act, and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-OCC-94-08) be, and hereby is, approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 94-32253 Filed 12-30-94; 8:45 am]

BILLING CODE 8010-01-M

[Release No. 34-35140; File No. SR-PSE-94-31]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by Pacific Stock Exchange, Inc. Relating to the Listing and Trading of Small Corporate Offering Registration ("SCOR") Securities on the Exchange

December 22, 1994.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on December 15, 1994, the Pacific Stock Exchange, Inc. ("PSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The PSE is submitting this rule filing in order to permit the Exchange listing and trading of common stock and preferred stock that qualifies under the Small Corporate Offering Registration ("SCOR") designation.¹

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Introduction

The Exchange is proposing to list and trade common stock and preferred stock that qualifies under the Small Corporate Offering Registration ("SCOR") designation. Under the proposal, the SCOR marketplace will be implemented on a three-year pilot basis and the program will be evaluated at least on an annual basis to determine whether this new marketplace has achieved its policy objectives—to facilitate capital formation for small businesses and to provide public market liquidity. The SCOR program will include any securities of an issuer that has been designated as common stock and/or preferred issued pursuant to (i) Regulation A under the Securities Act of 1933 ("Securities Act") and using the prescribed form as applicable; or (ii) Rule 504 under the Securities Act and using Form U-7 of the North American Securities Administrators Association ("NASAA") or a state variation of such form with substantially similar requirements.² Since such securities are not currently listed or traded on any national securities exchange, the PSE believes that the implementation of the Exchange's proposal will facilitate the capital formation process for small

companies and will supply much-needed liquidity to public investors within a regulated marketplace. In addition, under the proposal, companies will be afforded all of the benefits of an Exchange listing, with the exception of the Blue Sky exemption from state securities registration requirements and automatic marginability.

In August 1992, the Commission adopted certain rules as part of its Small Business Initiatives program. The program includes, in part, substantive changes to the "small issues" exemption from registration requirements under the Securities Act (Regulation A), as well as changes to the "seed capital" registration exemption pursuant to Rule 504 under the Securities Act. These revisions are designed to facilitate the access of small companies to capital markets and to reduce the costs of compliance with the federal securities laws.

Rule 504

The Commission's modifications to Rule 504 include the elimination of several restrictions and other changes that would allow small companies to conduct public offerings of up to \$1 million in unrestricted securities during a twelve-month period. These changes are designed to allow small companies to market offerings directly to prospective investors by bypassing both the venture capital and small underwriting houses. At the state level, offerings may be registered using the SCOR registration form, Form U-7; however, such limited offerings must also qualify under state Blue Sky laws that require delivery of a prospectus, offering circular, or disclosure document to all purchasers prior to sale. The Form U-7 has been supported by the American Bar Association as well as NASAA.³

Regulation A

The Commission revised Regulation A to exempt from registration public offerings of up to \$5 million in a twelve-month period. The disclosure requirements are embodied in the offering statement (SEC Form 1-A), which consists of three parts. The offering circular is contained in Part II and may be prepared in three alternative formats, one of which permits the use of the same simplified disclosure statement (Form U-7) that is prescribed by most states for SCOR offerings.

The Exchange believes these changes to Regulations A and D, in conjunction

⁷ 17 CFR 200.30-3(a)(12) (1994).

¹ The PSE originally proposed to list and trade SCOR securities in 1992. That proposal was published for public comment in Securities Exchange Act Release No. 32514 (June 25, 1993), 58 FR 35496 (July 1, 1993) (File No. SR-PSE-92-42). The Commission received several comment letters regarding the proposal, and subsequently published amendments to the proposal for public comment in Securities Exchange Act Release No. 34328 (July 7,

1994), 59 FR 35776 (July 13, 1994). The Exchange withdrew file no. SR-PSE-92-42 on November 22, 1994, and submitted the instant filing that includes modifications to the proposal in response to comments from the public and from Commission staff.

² Once a single issuance of securities has been accepted for listing on the Exchange, all securities of that class will be considered to be "SCOR" securities for purposes of this rule, including restricted securities (*i.e.*, securities restricted pursuant to federal or state securities laws, by any other law, by any agreement, or in any other manner), provided that such restricted securities may not be eligible for trading on the Exchange.

³ See Small Corporate Offering Registration Program and Form U-7, 1 Blue Sky L. Rep. (CCH) ¶ 6461 (September 1994).